

Issue Paper Number

99-040



BOARD OF EQUALIZATION
KEY AGENCY ISSUE

- ☐ Board Meeting
- ☐ Business Taxes Committee
- ☒ Customer Services Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Technology & Administration Committee
- ☐ Other

LOCAL TAX REALLOCATION INQUIRIES

I. Issue

At the June 29, 1999 meetings of the Board's Technology and Administration and Customer Services Committees, a local tax representative expressed concern about the administrative backlog of local tax reallocation inquiries pending in the Board's Allocation Group. The Board Members expressed similar concern and directed staff to address this issue at the August 31, 1999 Customer Service Committee meeting in Sacramento. The purpose of this issue paper is to review these concerns and develop a strategy for reducing the reallocation inquiry inventory to an acceptable level.

II. Staff Recommendation

In order to reduce the local tax reallocation inquiry inventory to an acceptable level the following two strategies should be adopted.

1. Increase the minimum dollar threshold with which local tax reallocations would not be recommended—to \$500 per reporting period.
2. Add, on a temporary basis not to exceed two years, 4 PY's (Associate Tax Auditors) to the Allocation Group to help reduce the inquiry inventory to a manageable level.

III. Other Alternative(s) Considered

Alternative 1:

The same as the staff recommended action, but without staff augmentation.

Alternative 2:

Advise the inquiring jurisdiction or consultant that only a finite number of reallocation inquiries can be processed each year, allowing them to prioritize those they want examined in the coming year or quarter.

IV. Background

Local tax revenues are distributed to local jurisdictions based on the taxpayer's return and remittance of the funds. Sometimes it is discovered after distribution that the tax was not reported or allocated correctly. Revenue and Taxation Code section 7209 provides that redistribution of the local tax can be made for the two quarterly periods prior to the quarterly period in which the Board obtains knowledge of the improper distribution.

The Allocation Group, organized under the Refund Section in the Headquarters Operations Division of the Sales and Use Tax Department, verifies local tax reallocation recommendations made pursuant to Board audits of taxpayer businesses. The group also handles analyses of local tax allocation inquiries filed by local jurisdictions and/or their authorized representatives.

In an effort to expedite the handling of reallocation inquiries, and also as a means of strengthening the internal controls over fund transfers that result from local tax reallocations, these functions were transferred to the newly created Allocation Group in December 1995. As of July 1996, when a computerized inventory of filed reallocation inquiries was revamped, the inventory of uncleared-filed inquiries numbered 3,205. Three years later, on June 30, 1999, the inventory backlog had increased 53 percent to 5,215 inquiries. An aging of these inquiries appears as Exhibit 1. The exhibit shows that 34 percent of aged inquiries are less than six months old while the remaining 66 percent of aged inquiries are six months or older. The oldest cases submitted by the two primary local tax representatives filing these inquiries have "dates of knowledge" of March 1989 and December 1993, respectively.

Some local jurisdictions have submitted their own local tax reallocation requests but the majority of the current aged inventory is attributable to inquiries filed by two consulting firms. As of June 30, 1999, consultant active inquiries totaled 4,904 (94 percent) of the total 5,215 inquiries held in inventory. City and/or county filed claims comprise the remaining 311 cases (6 percent) held in inventory as of that date. Exhibit 2 shows a breakdown of the number of inquiries filed by these parties over the period July 1996 through June 1999.

Discussion – Staffing and Productivity Level of the Allocation Group

The current staffing of the Allocation Group---one Supervising Tax Auditor I, eight Associate Tax Auditors, three Tax Auditors, and one Tax Technician III---has remained constant since August 1998.

The office performs two primary local tax functions: 1) responding to inquiries from representative consulting firms and local jurisdictions concerning possible misallocation of local tax and, 2) performing duties associated with reviewing the Forms BT-414-L which reallocate local tax as a result of audits of taxpayers with multiple outlets or who are classified as special sellers. Over the past three years the Allocation Group has assigned varying personnel to these duties depending on the workload volume associated with these functions. As of June 30, 1999, the Allocation Group had seven persons working the representative inventory and five persons handling the BT-414-L workload.

Over the past three years, the Allocation Group has worked and cleared some 13,373 inquiries, averaging 371 completed inquiries per month. This workload includes investigation of the less complex

tax area code (TAC) type inquiries--which on average take one hour to process--together with the more complicated inquiries--which on average require four hours to complete. There is currently no inventory backlog associated with the less complex tax area code inquiries so the current inquiry backlog relates exclusively to the more complex local tax cases.

Discussion – Volume of Local Tax Allocation Inquiries Received by the Board

Exhibit 3 displays the volume of inquiring jurisdiction or representative (IJR) inquiries received over the period July 1996 through June 1999. Although the aggregate volume of filed inquiries remains relatively high, this volume has not grown appreciably over the past three years. The exhibit shows the number of all IJR inquiries received on a quarterly basis over this period. Also shown is the average number of inquiries received per month from these sources. Data are not available on the number of city/county-filed inquiries prior to January 1999, but these are presumed to have remained constant over the reviewed period. City/county inquiries average 85 claims per month while consultant-filed inquiries average 350 per month. The aggregate average number of claims filed per month from all sources is 435 (350 + 85).

Discussion – Analysis of Personnel Years (PY) Required to Clear the Inventory Backlog; Normal Workload Inventory

Exhibit 4 details the number of personnel year equivalents necessary to clear the June 30, 1999 IJR inventory backlog, plus handle the anticipated number of new inquiries to be filed in the current and next fiscal year. Approximately 12.6 PY's would be required to clear this workload, 5.6 PY's more than is currently assigned to this work.

The analysis assumes that there would be a normal working inventory of four months' cases on hand at any given time ($4 \times 435 = 1,740$ cases). The four month work-in-process inventory appears reasonable based on the expected time lag between referring cases to taxpayers or district offices (45 to 90 days) and then allowing sufficient time for follow up or discussion of the inquiry with the IJR (minimum of 30 days).

Discussion – Minimum Reallocation Threshold and Staff Augmentation

Currently, the Allocation Group only approves authorized fund reallocations for local tax amounts exceeding \$50 per reporting period. Amounts not meeting this dollar threshold are denied because it is clearly not cost-beneficial to work such small requests. Because no minimum reallocation threshold is specified in the statutes, consideration has been given to increasing the \$50 threshold to a more realistic amount and, in the process, reducing the number of reallocation inquiries requiring adjustment.

It was originally believed that raising the threshold to \$250 would reduce the workload by 30%. In a review of consultant inquiries filed during the first quarter of 1999, however, it was determined by sampling that raising the minimum reallocation threshold to \$250, \$500, \$750, or \$1000 per reporting period would not have the dramatic impact previously expected on reducing the number of non-tax area code inquiries processed by the Allocation Group. Nevertheless, staff believes that raising the threshold

to a more cost-beneficial level makes sense from an administrative standpoint and will help reduce the backlog.

Discussion – Justification of Staff’s Recommendation; Funding Considerations

In order to address the growing inventory of uncleared IJR inquiries, staff recommends the adoption of revised administrative procedures that will allow for more efficient handling and clearing of local tax reallocation inquiries. While it is believed these improved procedures will enhance productivity and result in a corresponding reduction in the inquiry backlog, it also appears apparent that additional staffing is required to address the aged inventory in a timely manner. Consequently, staff recommends that the Allocation Group receive four 2-year limited term positions (Associate Tax Auditors) to help reduce the inquiry inventory.

The resources budgeted for the handling of Local Tax Allocation are funded through reimbursements from local government pursuant to Bradley-Burns statutes. Because the Board is prohibited from using resources budgeted for other than Local Tax Allocation, any proposals for resource augmentations for this activity would require an increase in the Board’s reimbursements authority and would require approval of the Director of the Department of Finance. Assuming the four positions were approved on a 2-year limited term basis, beginning January 1, 2000, the associated costs for these positions would be \$157,000 in FY 1999-2000, \$240,000 in FY 2000-01, and \$123,000 through December 31, 2001.¹

V. Staff Recommendation

A. Description of the Staff Recommendation

It is the staff’s recommendation that:

- 1) The staffing of the Allocation Group be augmented on a temporary basis with 4 PY’s (Associate Tax Auditors), for the lesser of two years or until such time as the backlog is brought up to date;
- 2) The Allocation Group’s procedures be revised to limit reallocation adjustments to amounts totaling \$500 and above per reporting period.

B. Pros of the Staff Recommendation

- Inquiry investigations of possible misallocation can be conducted in a timely manner as opposed to allowing the inquiries to continue to accumulate.
- Inquiries can be investigated early to validate possible misallocation while the information is current. Delay in conducting these investigations by any significant amount of time requires longer completion time due to the trail of information no longer being available or a change in taxpayer personnel.
- Provides local jurisdictions with local tax revenues due to them on a timely basis.

- Investigations can be completed within a reasonable period of time to minimize the delay in making reallocations to two or three quarters on the average. Delay in conducting investigations has the effect of extending the Statute of Limitations, which can encompass five to seven quarters reallocations, thus having a greater impact for the jurisdictions losing the allocation.
- Provides local jurisdictions with timely revenue corrections and information that will assist them with more accurate budgeting, keeping fluctuations to a minimum.
- Taxpayers operating without a permit or having unregistered sublocations can be identified on a more timely basis. This could potentially increase taxpayers' self reported tax, thereby increasing both state and local revenues.
- Reduces the number of errors in allocation of local tax revenues, which will improve the Board's service to local jurisdictions.

C. Cons of the Staff Recommendation

- Some jurisdictions that have gained revenues through inquiries may object to raising the reallocation threshold to \$500 per reporting period.
- If staff augmentation is sought, the reimbursable cost for four 2-year limited term positions (Associate Tax Auditors) is approximately \$157,000 for six months of the current fiscal year (1999-00), \$240,000 in FY 2000-01 and \$123,000 in FY 2001-02.¹

D. Statutory or Regulatory Change

None.

E. Administrative Impact

None.

F. Fiscal Impact

1. Cost Impact

The reimbursable cost to augment the BOE budget by four 2-year limited term positions is approximately \$157,000 for six months of the current fiscal year (beginning January 1, 2000), \$240,000 in FY 2000-01, and \$123,000 through December 31, 2001.¹

2. Revenue Impact

None.

G. Taxpayer/Customer Impact

Minimal impact.

H. Critical Time Frames

The Allocation Group should immediately begin using the revised reallocation threshold, and clearing those inquiries that do not meet this minimum level.

VI. Alternative 1

A. Description of the Alternative

This alternative is the same as staff's recommendation except that it would not include the request for 4 PY's (Associate Tax Auditors).

B. Pros of the Alternative Recommendation

This alternative contains the same advantages as staff's recommendations except that the current inquiry backlog would not be completed within as short a timeframe. Instead, under this proposal it is estimated that the current backlog would not be cleared for 8 years.

C. Cons of the Staff Recommendation

- Some local jurisdictions may object to raising the reallocation threshold to \$500 per reporting period.
- Some local jurisdictions may object to not having their filed inquiries cleared by the Allocation Group within the next 8 years.

D. Statutory or Regulatory Change

None.

E. Administrative Impact

None.

F. Fiscal Impact

1. Cost Impact

Cost would be minimal and absorbable.

2. Revenue Impact

None.

G. Taxpayer/Customer Impact

Minimal impact.

H. Critical Time Frames

The Allocation Group should immediately begin using the revised reallocation threshold, and clearing those inquiries that do not meet this minimum level.

VI. Alternative 2

A. Description of the Alternative

Advise the inquiring jurisdiction or representative that only a finite number of reallocation inquiries can be processed each year, allowing them to prioritize those they want examined in the coming year.

B. Pros of the Alternative

- Does not require new resources to handle consultant inquiry workload.
- Offers IJR's the option to prioritize those claims they want examined in a given year.
- Over time, this methodology will clear the inquiry backlog.

C. Cons of the Alternative

- IJR's do not normally know the amounts of local tax subject to reallocation so it could be difficult for them to prioritize their inquiries.
- Limiting the number of claims eligible for review each year may be seen as too restrictive to some IJR's.

D. Statutory or Regulatory Change

None.

E. Administrative Impact

Changes the method for determining which inquiry claims will be worked first. Will assist in reducing the inquiry workload to a normal working level.

F. Fiscal Impact

1. Cost Impact

Absorbable.

2. Revenue Impact

None.

G. Taxpayer/Customer Impact

Would impact the way reallocation inquiries are referred to the agency. IJR's would be encouraged to prioritize those inquiries to be handled each year; otherwise the cases would be worked on a first-in-first-out basis until a predetermined limit was reached.

H. Critical Time Frames

None.

Prepared by: Program Planning Division

Current as of: September 2, 1999

¹ The cost estimates for the four 2-year limited term positions have been revised since this paper was issued on August 30, 1999. The costs were originally estimated as \$158,000 in FY 1999-2000, \$240,000 in FY 2000-01, and \$158,000 through December 31, 2001.

Aged Inventory:
Consultant and City/County Filed Inquiries
As of June 30, 1999

	A	B	C	D	E	F	G
1							
2							
3	Inquiry		Consultant		City or		
4	File Date		Inquiries		Inquiries		TOTAL
5	(By Quarter)		6/30/1999		6/30/1999		<C+E>
6							
7	4-95 & Pr.		499		0		499
8	1-96		67		1		68
9	2-96		35		0		35
10	3-96		30		0		30
11	4-96		221		0		221
12	1-97		57		0		57
13	2-97		195		5		200
14	3-97		261		6		267
15	4-97		317		7		324
16	1-98		282		2		284
17	2-98		440		13		453
18	3-98		507		10		517
19	4-98		462		17		479
20	1-99		1013		32		1045
21	2-99		518		218		736
22							
23	Total		4904		311		5215
24							
25							
26							
27							
28							
29	Comments						
30	The above identifies the inventory of inquiries received by the calendar quarter received.						
31							
32							
33							
34		Consultant and City/County Filed Inquiries:					
35		Aging Schedule as of June 30, 1999					
36			Consultants	City/County		Combined	Percentage
37		0-59 days	518	211		729	
38		60-119 days	708	24		732	
39		120-179 days	305	15		320	
40		Subtotal < 6 months old	1531	250		1781	34%
41							
42		180 days and over	3373	61		3434	66%
43							
44		Grand Total	4904	311		5215	100%
45							
46							
47							

Allocation Group:
Reallocation Inquiry Inventory
Summarized By Quarter

	Period											
	3Q-96	4Q-96	1Q-97	2Q-97	3Q-97	4Q-97	1Q-98	2Q-98	3Q-98	4Q-98	1Q-99	2Q-99
All*	3,411	3,369	3,470	3,473	3,352	3,741	3,987	4,291	4,777	5,019	5,192	5,215

**Consultant
Inquiries**

Beg. Inv.	3,205	3,411	3,369	3,470	3,473	3,352	3,741	3,987	4,291	4,777	4,739	4,880
New Inquiries	946	1,081	962	920	940	1,093	1,215	1,524	1,173	971	929	867
Inquiries Completed	740	1,123	861	917	1,061	704	969	1,220	687	1,009	788	843
Ending Inv.	3,411	3,369	3,470	3,473	3,352	3,741	3,987	4,291	4,777	4,739	4,880	4,904

**City/County
Inquiries****

Beg. Inv.											280	312
New Inquiries											264	247
Inquiries Completed											232	248
Ending Inv.											280	312

* Reflects the inventory balance of all uncleared inquiries (consultant and city/county inquiries included).

** The available history for city/county inquiries covers the last six months of FY 98/99.

Allocation Group:
Average Number of Reallocation
Inquiries Received Per Month

	A	B	C	D	E	F	G	H	I	J	K	L	M	N
1	Inquiries Received Over the Period July 1996 Through June 1999													
2														
3														
4														
5	Source of	QUARTERLY PERIOD												
6	the Inquiry	3Q-96	4Q-96	1Q-97	2Q-97	3Q-97	4Q-97	1Q-98	2Q-98	3Q-98	4Q-98	1Q-99	2Q-99	Total
7														
8	Consultants	946	1,081	962	920	940	1,093	1,215	1,524	1,173	971	929	867	12,621
9														
10	Total	946	1,081	962	920	940	1,093	1,215	1,524	1,173	971	929	867	12,621
11														
12	Avg. # of Inquiries													
13	Received													
14	Per Month													
15	(Line 10/3)	315	360	321	307	313	364	405	508	391	324	310	289	350
16														
17														
18														
19	Source of	QUARTERLY PERIOD												
20	the Inquiry*	3Q-96	4Q-96	1Q-97	2Q-97	3Q-97	4Q-97	1Q-98	2Q-98	3Q-98	4Q-98	1Q-99	2Q-99	Total
21														
22	City/County											264	247	511
23														
24	Total											264	247	511
25														
26	Avg. # of Inquiries													
27	Received													
28	Per Month													
29	(Line 24/3)											88	82	85
30														
31														
32	Average Number of Inquiries Received Per Month From All Sources (Line 15 + Line 29)													435
33														
34	* Data for city/county inquiries only available for the period January 1999 through June 1999.													

Allocation Group:
Analysis of Personnel Years:
2 Year Plan to Clear Inquiry Backlog

		TAC 40%	OTHER 60%	Total Hours	PY's @ 1800/yr
2 YEAR PLAN					
Backlog As of 6/30/99	5,215		5,215		
New Inquiries: FY 1999/00 (435x12)	5,220	2,088	3,132		
New Inquiries: FY 2000/01 (435x12)	5,220	2,088	3,132		
Sub	15,655	4,176	11,479		
Hours per inquiry		1	4		
Hours required to process Inquiries		4,176	45,916	50,092	27.8
Less:					
4 mo. working inv. adj. (435 x 4)	1740	696	1,044		
Hours per inquiry		1	4		
Hours required to process		696	4,176	4,872	
Net hours required over 2 years				45,220	25.1
Net hours required per year				22,610	12.6

Comments

The estimated percentages of tax area code (TAC) and Other Inquiries was derived from historical submissions.

The estimated hours to complete the TAC & Other Inquiries (1 & 4 hours, respectfully) was derived from a review of actual cases worked.

		TAC 40%	OTHER 60%	Total Hours	PY's @ 1800/yr
REQUIRED PY's TO STAY CURRENT					
New Inquiries per year (435x12)	5,220	2,088	3,132		
Hours per Inquiry		1	4		
Hours required to process		2,088	12,528	14,616	8.1
Current staff working Inquiries					7.0
Additional staff needed to stay current					1.1

REQUIRED PY's FOR BACKLOG

Total workload PY's per year (as calculated above)	12.6
PY's to stay current (as calculated above)	8.1
Additional staff needed for backlog	4.5